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Western Corporate Forms and the Social Origins of Chinese Diaspora Entrepreneurial Networks

Wai-keung Chung

Introduction

It is undebatable that the economic growth of the last few decades in Southeast Asia can largely be attributed to the business activities of the Chinese diaspora.[1] The ethnic Chinese, who constitute fewer than 10 per cent of the population in Southeast Asia, hold a significant proportion of its wealth. While different perspectives are available to explain this economic miracle created by the Chinese, one major argument is that the success of the Chinese can be attributed to their unique pattern of business organization. This pattern of organization has created what some scholars would call a ‘network-based economy’, as opposed to a ‘firm-based economy’ that is commonly found in many Western economies.[2]

A network-based economy is an economy based on relational networks – economic actors connect to each other through various personal networks. Because of the functionalities of the networks, it is the networks, rather than the individual firms, that are the key contributors to the economy. Firms, in this case, are therefore embedded in networks. Conversely, in a firm-based economy, there are individual firms in the market that are competing with each other to maximize their profits. Firms are the key contributors of the economy, and networks, if they ever exist, are secondary. Through legal individuation of economic actors, networking becomes a functional strategy between individual firms. Networks, in a firm-based economy, are therefore embedded in firms.

A typical Western economy develops an institutional foundation that facilitates autonomous individual economic actors, therefore facilitating a firm-based economy; Asian economies, notably Chinese, Japanese and Korean economies, are rooted in social and economic institutions that encourage personal ties and network formation.[3] With different institutional settings in the societies, the organizational logics of the economies will be different.

This chapter provides a socio-historical analysis of the emergence of the network-based economy among the Chinese business communities in Southeast

Asia. I argue that fundamental characteristics of post-Second World War Chinese diaspora economic activities can be traced back to both the long history of Chinese business practices and to the institutional transformation of the Chinese economy since the turn of the last century. Modern organizational logics of the economy developed in Mainland China beginning in the early twentieth century, and spread overseas along with the development of overseas Chinese communities.[4] While local factors were also crucial in shaping particular business strategies of overseas Chinese in different Southeast Asia countries, their general practices were influenced by Mainland China (Limlingan 1986). After all, we can see a general pattern of business practices from the Chinese entrepreneurs in Southeast Asia that are consistent with practices in other Chinese communities, including Hong Kong and Taiwan.

I will first discuss the basic features of the Chinese diaspora entrepreneurial networks in Southeast Asia and the social mechanism behind their business practices. Personal trust based on social norms, rather than contracts backed by a legal system, is the key component of these very adaptive entrepreneurial networks, working both within and among Chinese communities in Southeast Asia. I will then illustrate the socio-historical origin of the network-based capitalism created in China. The origin of this network economy can be traced back to the late Qing economy in the nineteenth century. The institutional transformations initiated by the introduction of Western corporate forms during that time eventually changed the economy – they transformed traditional business networks by preparing the business community for a fundamental structural change, and through the process created a new setting for the rise of Chinese entrepreneurship. Rather than being replaced by the economic mechanism of Western capitalism during the transition, the use of personal networks survived by reinventing itself, and has since remained a vital element of the overseas Chinese economy.

Chinese Diaspora Business Networks in Southeast Asia

Ethnic-specific networking as a business strategy can be found in many societies where overseas Chinese are conducting economic activities. Research indicates that ethnic ties among overseas Chinese are particularly crucial in capital formation and information flow (Weidenbaum and Hughes 1996). While the impact of this ethnic-based networking among Chinese can be found in many places around the world,[5] the role of Chinese capital and its contribution to local economies in Southeast Asia has attracted particular attention since the 1980s (Lim and Peter 1983).[6]

Being referred to as the 'Lords of the Rim' (Seagrave 1995), 'Merchant Princes' (Hodder 1996) and 'Essential Outsiders' (Chirot and Reid 1997) of Southeast Asia, it is undeniable that overseas Chinese have made their mark in this part of the world. The Chinese played a leading role in the economic life of different parts of Southeast Asia as early as the seventeenth and eighteenth centuries (Trocki 1997; Yoshihara 1988). Economic activities in Southeast Asia have since then proliferated largely because of Chinese settlement in the region. In recent years, elite Chinese entrepreneurs in East and Southeast Asia have increasingly engaged in multi-million-dollar joint ventures (Redding 1995). Liem Sioe Liong of the Salim Group in Indonesia, Robert Kuok of the Kuok group in Malaysia, Chin Sophonpanich of the Bangkok Bank Group in Thailand, to name a few, have all contributed to the economies of the countries where they reside, and at the same time have formed joint ventures among each other that have contributed to the regional prosperity. Informal linkages between regions and countries through the ethnic ties of the Chinese have contributed to an integration of the economies in the Southeast Asia region (Peng 2002).[7]

This kind of inter-country economic activities would happen much less frequently without the informal personal ethnic-specific ties, especially since the legal framework for international business transactions within Southeast Asia is weak (Rauch and Trindade 2002).[8] The creation of these ethnic-specific networks is based on a social mechanism existent in all Chinese communities, to different extents, that guarantees the relative advantage of using personal connections as social capital in business transactions.[9]

The Social Foundation of Network Economy

A network economy is an economy that is based on personal connections backed by social trust; and trust is being confident that your trustee is not going to engage in opportunistic behaviour even though it is in his or her own best interest. A social trust is one that is regulated by social norms, rather than by an authoritarian third party, typically the government. Chinese business transactions have long been depended on as a trust-based, self-regulated mechanism. For centuries, Chinese society had developed sets of norms and rules that could guarantee an acceptable degree of certainty in economic transactions and which had never been replaced with any institutional alternative.[10]

Business transactions among overseas Chinese, including Southeast Chinese, depend on the same social foundation that has evolved in China after centuries of commercialization. It is a practice that is based on personal trust which allows non-contractual business exchange. Personal trust among Chinese is built on the assumption that there is a shared moral culture of honesty that is expected to be the ethical code of anyone doing business. To be a Chinese, or even better, to be someone from the same native place, is advantageous in that it assumes a mutual expectation of honesty between each other and therefore a good partnership.

The reasons why Chinese businessmen prefer non-contractual rather than contractual relationships are not simply based on a lack of contract tradition in China, or the fact that there is no institutional support for the contract.[11] More importantly, it is the availability of a social-trust mechanism that can guarantee the reliability of a non-contractual relationship, which in turn allows the kind of flexibility that the Chinese businessmen may actually prefer to have as a strategy to tackle the ever-changing market situation. Accordingly, trust is not just for risk and uncertainty reduction, it is also essential for the transaction to be more predictable, efficient and flexible.

Organizational studies on inter-firm relationships suggest that the availability of trust can be a positive source of competitive advantage if it can be maintained (Barney and Hansen 1994). A trust-based transaction is supposed to be more flexible and efficient (Nooteboom et al. 1997; Uzzi 1996, 1997). In a transaction that is based on pre-existing *guanxi* – personal relationships – between two business parties, business decisions can be made more quickly than transactions that are based on contracts since an informal phone call may be all that is required to solve a business problem (Chen 1994; Yao 1987).[12] A 'loose' contractual form – or even a verbal promise – can often be more cost-effective than a written legal form, provided there is a personal trust to guarantee it (Charny 1990). If the exchange is based on a contract rather than mutual trust, it will be less flexible to change, and will be slower and more costly to alter the terms to respond to external fluctuations of conditions.

This kind of flexibility is significant especially for the small- to medium-sized manufacturing enterprises that are commonly found in East and Southeast Asia. Smaller manufacturers have to respond to the changing market in a quicker and more flexible way. In order to survive, they have to be flexible enough to capture different kinds of business opportunities. What they may prefer are business partners who can be flexible and willing to cooperate when specific needs of production or services arise. The economic opportunities that are created through these flexible and cooperative relationships are difficult to replicate via markets, contracts or vertical integration (Uzzi 1997). The choice of flexibility might be a rational one, but to fulfil this choice one has to depend on the embedded norms that govern the social relationships of Chinese society. Seeking flexibility in a business transaction therefore may be less feasible in a Western context, or at least it requires a totally different social mechanism to achieve it.[13]

Particularly in overseas Chinese communities, people from the same native place are expected to be closer to each other than Chinese from other communities, as native fellows have a higher density of social connections back home. Groups with a high density of overlapping relationships can establish an internal mechanism through invisible codes of ethics to maintain a higher level of trust among the group members (Landa 1994). Also, the relative interconnectedness of every individual with other group members will facilitate positive personal traits such as greater sense to exhibit reliability and sincerity among the group members, since if these traits are not kept, most people within the group will know it. The existence of groups with overlapping relationships traditionally provided some guarantee for those doing business within the network.[14] *Tongxiang,* or the native fellows, among Chinese who share a common dialect and collective memory of their hometown, find it easier to create social ties with each other.[15] While their decisions were based on business, the fact that both Robert Kuok of Malaysia and Liem Sioe Liong of Indonesia are Hokkien and speak the same dialect certainly helped to establish the cross-border joint ventures between them.

The use of *guanxi* in Chinese business practices therefore facilitates inter-firm transactions in the Chinese business community. Rather than making transactions of various kinds through arm-length relationships, Chinese entrepreneurs tend to seek business partners whom they can trust. Networks of firms are created among Chinese entrepreneurs through the *guanxi* social logic. In the Chinese business context, a network is the resulting configuration of a set of *guanxi*. It represents the structure of how a person relates him/herself to a group of people through personal connections. Chinese networks in general can be used to avoid opportunistic behaviour by mutual trust without using costly monitoring apparatus. For Chinese firms, trust-building seems to be less of an issue, although it is certainly cannot be said that there are no problems establishing trust among Chinese firms, as dishonesty happens everywhere. Trust in Chinese societies, however, as different from that of the West, is supported by a moral community who sees the practice of *guanxi* logic and trust as a 'normal' and 'expected' social practice among those who are related. Daily-life experience, which emphasizes sincerity and honesty, has given every individual a shared understanding of what is trust, how to be trustworthy and how to interpret another's actions in terms of trustworthiness, even if one does not intend to practice these social conventions. This common cultural awareness and practice of trust has facilitated the establishment of trust among business partners.

The interconnectedness of Chinese firms in Southeast Asia, as in other Chinese communities, also becomes an essential tactic for the growth of their firms. In typical Chinese family firms, top management positions are always filled by family members, and sometimes close relatives or employees who have been working for the family for decades. One of the common critiques of Chinese business practices is the closed system of its decision-making process, which in turn can limit the growth of the firm. In the past, most Chinese firms were small- to medium-sized, and indeed were limited by their own management style. However, the Chinese family firms typically found in Southeast Asia have overcome their scale limitations by networking with other Chinese family firms, not just within their place of residence, but also beyond to other parts of the region (Hamilton 1996a; 2000; Redding 1995).

A well-established trust-based business *guanxi* can, therefore, serve as a preset channel of business transaction where both sides are willing to do business on a personal basis. Here we see a 'moral' contract in contrast to a legal one, between the two parties, one which represents a tacit agreement on any transaction. In this sense, business networks represent an extension of social networks. This socially-based business network then can provide access to credit, market information, services and trading opportunities, etc., which makes Chinese firms more competitive. The connections of firms turn them into much bigger business entities with a combination of the resources from this collection of firms. Family business, as the most typical organizational form of Chinese business, can therefore benefit from this networking strategy to increase its competitiveness by increasing its opportunities and flexibility. Personal relationships can turn into a direct joint-investment relationship, e.g. joint-family business, or if not, at least can be a supportive network for one's business.

Chinese business networks are an extension of social networks. This social nature of Chinese networks is supported by the *guanxi* logic that every Chinese, including those overseas, practices on a daily base (Chung and Hamilton 2000). Social logic is used to maintain and strengthen business networks.[16] Even though some may do better than others, every Chinese has the shared understanding of the logic on how to relate to others. On the contrary, in the American business community, for example, networking basically represents a learned behaviour with little social basis. Western business networks may also be an outgrowth of one's social network, since a firm's prior social ties can help to identify alliance partners and opportunities (Gulati 1998), but the social dimension ends there, the remainder typically being replaced by business logic. [17] Personal trust, if it ever exists in a typical Western context, will remain at the personal level between the involved parties and will not be monitored by any social mechanism.

Traditional Chinese Business Networks

These business practices and their related social dimensions can be identified in almost every Chinese community. The practice of network economy has a long history in China and can especially relate to the 'traveller economy' in the traditional Chinese economy. Merchants from all parts of the country travelled to different locations and did business in that location much like a diaspora community. They had to face a high level of uncertainty in places that were 'foreign' to them. Networks in the traditional Chinese business community were used to extend business opportunities, and more importantly, to stabilize the transactions. Merchants from the same native place who settled in the same location were connected together through native-place associations and professional guilds where regulations would be set and reinforced to regulate the business. Traditional networks, while helping individuals to maximize the utilization of one's business opportunities, were at the same time promoting cooperation among those who were linked.

Chinese Native Banks as an Example

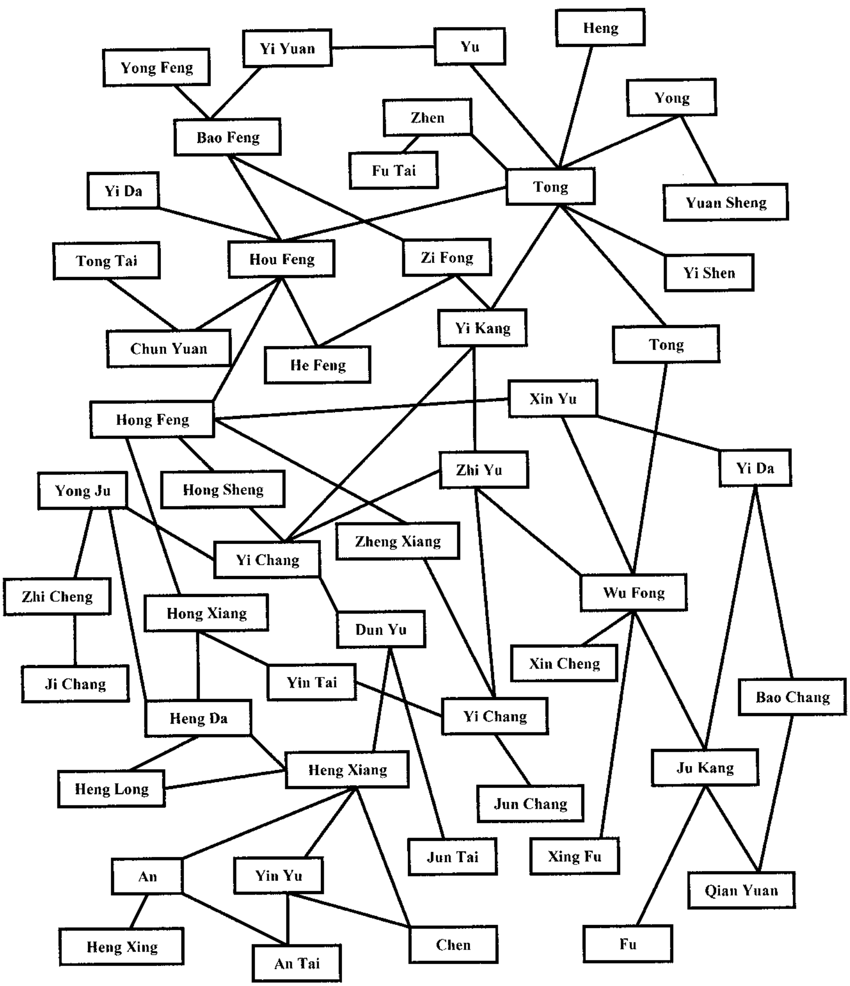
The organization of native banks (*qian zhuang*) in modern China provides a good example of how traditional networks worked in late nineteenth- and early twentieth-century Chinese economy. Serving as the principal financial institution in China's advanced commercial economy during late imperial times, Chinese native banks were among the most traditional forms of Chinese business. Through an ownership analysis of all native banks in Shanghai during 1927, we can see how these native banks stand out as vibrant examples of how interpersonal networks function in a traditional Chinese business setting.[18]

Native banks normally provided services to a known group of merchants and tradesmen.[19] Wealthy merchants who had some capital to invest and many good connections in the commercial community usually started the banks.[20] Although a few were single proprietorships, most native banks were organized through partnerships of four to six people.[21] In most cases partners would have no kinship ties among them and instead would be predominantly friends and business colleagues of the same native place. Reputable individuals from outside the native regions who possessed good business contacts, possibly linked to foreign and Western-style modern banks, were also involved. In Shanghai, the guild of native banks linked all the banks together to form an overarching financial network that guaranteed and ensured the continuity of commercial transactions in the City.

A key characteristic of native-bank investment was cross-investment patterns. Rather than investing one's capital in only one place, as a sole proprietor for instance, native banks' investors would rather diversify their investments in different banks than place all their money in one bank. Partnerships created from such cross-investments neither created nor reflected a core business elite in each location. Rather, these partnerships represented interpersonal networks allowing investors to bridge multiple and distinct groups within the commercial community.[22] Native-bank organizers would also solicit partners who could bridge some of the regional cleavages that existed in most immigrant urban settings.

The operating capital of the native banks was usually quite small.[23] Different from modern Western banks which required very large pools of capital to support and guarantee business operations, Chinese native banks depended more on reputation as an asset and on personal ties as a guarantee. Partnerships in the Chinese native banks thus represented not only a pooling of capital, but also sets of relations that could potentially be tapped by each partner.

The membership list for the Shanghai native-bank guild provides information on partnerships for seventy-eight native banks operated in Shanghai during 1927. Only five of the seventy-eight native banks were sole proprietorships. The rest were formed by partnerships. Because of cross-ownership, most of the banks were directly or indirectly linked up with each other. Representing by a line between two banks when there is at least one interlocking ownership, Figure 13.1 shows that fifty of the seventy-eight native banks were linked through cross-ownership. This web of relations represents the personal linkages of individuals in Shanghai's



Source: Shanghai Native Banks Guild membership list 1927

Figure 13.1 Shanghai Native Banks Partnership Networks in 1927 native-bank community. The linkages facilitated a very efficient flow of market information which was essential for this banking institution.

This pattern of interlocking demonstrates a collection of 'weak ties' to create an extensive interpersonal network across Shanghai's native banks. Most of the interlocks are singular, i.e. no more than one partner has cross-investment in the same two banks and there appear to be no family groups represented among the interlocks. Rather than forming into one closed group, native-bank investors extended their connections by linking themselves directly and indirectly to multiple groups of people which in turn provided the foundation for native banks to operate as a financial system.

The system, which functioned without the intervention of state officials or the state's legal framework, worked quite well until after the Second World War.[24] Partnerships were made on the basis of unlimited liability, and bank loans were unsecured. The entire system operated on the basis of reputation: the banks' reputations, the partners' reputations, and the borrowers' reputations or that of their guarantors.[25] The system worked because the entire commercial community acted as third-party monitors backing every transaction. Information about misdeeds on the part of merchants or banks would circulate throughout the community, making it impossible to do business again in the community.

Since trust among banks was so important for the maintenance of the efficiency and stability of this traditional financial institution, native banks relied on a collective mechanism to guarantee the trustworthiness of the system: the local association of native bankers. Associational membership was monitored closely. To be a member of the guild, a bank needed to invite a person of high prestige within the community to serve as its guarantor. One's native-place origin was also very important. While there was never a rule restricting anyone from entering the business, the majority of the native banks' owners were from Ningpo and the surrounding areas. Ties based on native-place origin were certainly used as a tool to monitor and control this high-risk business.

Personal ties served at least one more function for native banks. When a bank began to run out of cash, for example when it issued more bank notes than it could afford to clear, the bank would have to ask for help from other banks with which they maintained connections. Personal ties helped to establish these 'strategic alliances' so that the amount of operating capital could be minimized and the chance of long-term survival maximized.

The nature of the traditional economy as illustrated here is that networks represent a web of mutual trust across a group of interrelated people. This web serves as a web of capital and information flow on the one hand, but also as a vehicle to exercise control and regulation from which the larger group can benefit. There was no centre within this kind of network. While there were merchants who were doing better than others, they were still supposed to be subordinate to the broader networks that encompassed people from the same native place, or people doing the same business. The operation of the native bank illustrates that personal ties were necessary for a merchant to get into the bank business, but the same ties also acted as a constraint on one's business conduct. So long as one was a member of the guild, one was supposed to conform to the rules and regulations set by the group. The networks in a traditional business community therefore performed the function of guaranteeing the stability and functioning of the business through which conformity to the group norms could be reinforced.

What we find among contemporary overseas Chinese communities, however, is a rather different kind of network. Originating from the traditional mode, the 'modern' network has become more 'personal'. Individual entrepreneurs, while attached to the networks, now can have more personal influence on how these networks will be created. These are not networks above individuals; rather, these are networks over which individuals have more control. I argue that this personalization of Chinese business networks was largely a result of the adoption of Western corporate forms, which eventually became an institutional device for individual entrepreneurs to consolidate their social capital into one legally independent entity.

The Transformation of the Traditional Chinese Economy

One could argue that the reason why contemporary Chinese are still using personal networks in economic transactions is that the Chinese economy has never been 'modernized'. Economic and legal institutions which are comparable to those in the West have never developed well. The continuous use of personal networks results from the fact that better alternatives do not exist. While this has some truth, the Chinese economy did transform itself by following a Western model with the development of Western-style institutions. The traditional business networks described above began to change gradually in the early twentieth century when Western ideas of business organization were more widely adopted.

Since the mid-1800s, foreign economic invasion had been progressively destroying the traditional economic system in China (Richardson 1999). Foreign goods were replacing traditionally domestic-made goods in many major sectors (e.g. textile). Foreign companies, involved at the beginning mostly in trading and finance but later on also in manufacturing, increased in number over time and put tremendous pressure on China's economy. This extreme competition had stimulated enormous discussion among the government, intellectuals and the business community in China, and had fostered tremendous institutional changes (most of which can be described as Westernization) in the economy which had never occurred before in Chinese history.

In the late nineteenth century, there was a shared belief in China that in order to increase national strength, commerce had to be developed and modernized, and in order to develop commerce, the economy should be organized under Western-style corporate forms (Guo 1995; Zhu 1996). In order to compete with their foreign counterparts, Chinese merchants mobilized to join together and establish *gongsi* (company). The introduction of corporate forms into China, especially the corporate form with limited liability, constituted a key landmark on the capitalistic transformation of the country's economy. The early stages of Chinese capitalism can therefore be characterized partly by the ways Chinese merchants reorganized themselves into companies in order to capture capital and to regain control of the national market. New business and organizational concepts such as the board of directors, shareholders, the general meeting, and limited liability, etc. were introduced into China and gradually changed the contours of commercial life in China.

China Incorporated

The result of this institutional transformation in the economic sector, however, was not as progressive as expected, and one could argue that the introduction of corporate forms and the related institutional transformation (e.g. legal reform) were not very successful. In terms of the number of firms registered as companies under the company law, the transformation was not significant. Between 1904, the first year of the promulgation of the first Chinese company law in China, and 1912 (end of the Qing Dynasty), the total number of registered companies was less than 200. There were only 1,185 more companies registered as limited companies between 1912 and 1927 (Shanghai Municipal Archives 1996). Compared with what happened in Britain, for example, where thousands of companies registered in the first few years after the liberalization of the limited-liability company and have increased rapidly in number since then, China did not experience such rapid growth in company establishment after the introduction of company law and there was no immediate effect on the organization of the Chinese economy.

However, when we look at the history of the emergence of corporate forms in the West, it appears that it actually took a few centuries for the company form to mature and become accepted by the public. It took about two hundred years for the joint-stock company to develop before it finally acquired its legal status in the 1800s and further developed into its mature form (Scott 1910). Without a long tradition of joint-stock business operation in China, it is only reasonable to expect that the Chinese would take some time to accommodate to, and to understand, this new institution before they would be more willing to adopt it.

Based on the statistics that are available, however, it is clear that a transformation of how business was organized did indeed happen in China, and that the sort of capital accumulation which characterized a modern economy did occur over time. Table 13.1 shows that there was an increase in the size of corporations' capital size from 1915 to 1920. Companies with a capital size of more than 1 million yuan (the Chinese currency at that time) composed only 2.3 per cent of all registered companies in 1915, but had jumped up to 8.6 per cent in five years.

Table 13.1 Percentage Distribution of Investment Capital Size in Corporations (in yuan)

	10,000–50,000	*50,000–200,000*	*200,000–500,000*	*500,000–1,000,000*	*1,000,000 and above*	*Total*
1915	31.9%	57.8%	6.0%	2%	2.3%	100%
1920	24.4%	49.6%	12.4%	5%	8.6%	100%

Source: Chen (1989: 261) (modified)

The global economic conditions during the First World War were very favourable to China. Institutional reform had benefited from this and had created a 'golden age' for Chinese capitalists (Bergère 1989). Accumulation and investment in the 'new economy' – the industrial production – had increased a few fold in less than a decade (especially between 1914 and 1921; see Table 13.2).

Table 13.2 Rate of Increase in Private Industrial Investment (in 10,000 yuan)

Industry	*1913*	*1921*	*Growth Rate (%)*	*Average Annual Growth Rate (%)*
Cotton Spinning	1,423	9,842	691.6	27.35
Flour	885	3257	368.0	17.69
Silk Reeling	1,603	2253	140.6	4.00
Tobacco	138	1,680	403.2	15.13
Cement	294	746	308.8	12.34
Matches	294	746	308.8	12.34
Total	4,628	18,658	403.2	19.04

Source: Huang and Yu (1995: 114) (modified)

While the statistics indicate that the total number of companies established per year was not impressive, they do suggest that the limited liability company was the most preferable organizational form. More than 70 per cent of those who registered between 1929 and 1935 were in this form. Even more significant is that the capital size of the limited-liability company was always much larger than that of other corporate forms. We can therefore argue that even though most economic activities were still conducted through traditional partnership or sole proprietorship, a significant percentage of national capital was incorporated.

The Emergence of Chinese Entrepreneurs

The way that the Chinese business community was organized started to experience changes at about the same time as the 1904 Company Law was officially introduced to the public. While traditional merchant organizations continued to exist for a longer time, new forms of business associations began to emerge at the turn of the century. The major change was the transformation of traditional business associations into modern, Western business associations like the Chamber of Commerce.[26] One of the later developments of the Chambers of Commerce in China was the further relaxation of membership criteria. This change signalled the emergence of relatively independent economic actors in the Chinese economy.

The Shanghai General Chamber of Commerce, as the most influential chamber of commerce in early twentieth-century China, gives us a representative example of this change. Its membership at the beginning was composed mostly of traditional merchants with gentry-status from different places of origin and different businesses. With representatives from only a few key Chinese enterprises, most of the members were representatives from guilds and trade associations (Xu and Qian 1991). In 1912, the association was reorganized into a more mature form – the Shanghai Chamber of Commerce. One of the major changes in this association was that the regulations on membership had been largely revised. The annual membership fee was significantly lowered from 300 *taels* of silver to 100 *taels* which eventually led to a broadening of membership to include individual members outside the traditional guilds and associations. More and more enterprises formed as companies became members of the Chamber. Younger elites from the new entrepreneur class also finally took more control in this modern Western business association.[27]

The impact of the emergence of this modern form of business association was the breakdown of traditional organizational patterns of the economy. The traditional structure of the business community was organized into sectors from different native places and different businesses. Since most traditional businesses were dominated by people from a particular native place, cross-sector investment was not common unless it was a business that one's fellow-regionals were also conducting.[28] Ties between each business (and each native place) were relatively tight. The changing composition of the chamber of commerce reflected the changing structure of the economy with more and more business activities being conducted by individual firms, and cross-investment becoming less restricted as a practice. At the same time, the proliferation of the chambers of commerce in China at the same time at least partly led to a structural change in the business community. It was a transformation that signified the emergence of modern firms in the Chinese economy.

As discussed previously, traditional merchants were supposed to be embedded in business networks rather than existing as individuals. Individual merchants were always recognized as part of a larger group – a *bang* or trade coalition. The social recognition of merchants in the past was based on where they were from or what business they were in and very little on who they were as individuals. Merchants from the *Jin* region – the Shanxi province – of China would be *Jin* merchants and were embedded in the *Jin* merchants' networks. Merchants who traded tea would be tea merchants and were embedded in the tea traders' networks. As part of a larger group, merchants were expected to be cooperative and not compete with each other. Rules and regulations were set by associations of their professions and high conformity was expected as a way to guarantee the stability of trade. No matter how successful the merchant was, he was expected to be subordinate and conform to the networks to which he belonged. Since business opportunities were highly constrained and regulated by guilds or trade associations,[29] opportunities for the emergence of business elites and expanding businesses were rare.[30]

Because of the changing institutional settings in the late nineteenth and early twentieth centuries, merchants were allowed to free themselves from traditional constraints and to engage in competition rather than cooperation. In contrast to the traditional merchants who were confined to those traditional businesses, 'new-style' merchants during the turn of the last century were referred to as merchants who invested in 'new-style' enterprises – manufacturing, banking and finance, public utilities, etc. The social consequences, however, were more than just alternative patterns of investment. Those who invested in these modern businesses were at the same time more likely to use Western corporate forms to organize their businesses and therefore much less likely to be confined by the traditional guild-related economy. Chu Baosan, for example, was one of those who had successfully transformed themselves into modern entrepreneurs by engaging in a diversity of modern businesses organized in Western corporate forms. He had been involved in forty-nine different companies, mostly as founder or co-founder, ranging from public utilities, mining, shipping, manufacturing and insurance to banking over the course of twenty-five years (Tao 2000). Liu Hongshen's business conglomerate, as another example, was organized as a group of related limited-liability companies that had diverged investments into a wide range of modern businesses – harbour, matches, cement, wool spinning, coal mining, enamel, banking and insurance (Shanghai Shehuikexueyuan Jingji Yanjiusuo 1981). Modern corporate forms that assume regulation from the government rather than from the guilds had helped Chinese merchants to break the traditional ties which promoted more cooperation than competition.

Firms as Carriers of Personal Resources

The adoption of corporate forms to establish one's business typically occurs because the design allows easier capital consolidation and at the same time offers relevant legal protection according to company law. In China, however, the introduction of this Western institutional design served more than that purpose and had turned out to be a *carrier* of personal resources – a device that made personal resources much more effective. To a large extent, the availability of this institutional device facilitated the emergence of business elites in China.

It is certainly true that it was engagement in modern businesses in China that allowed the creation of much greater wealth for modern businessmen in comparison to that of those who engaged in traditional businesses. And corporate forms, especially the form of the limited-liability company, became the most obvious choice for the organization of those modern businesses, as a larger amount of capital was usually needed. This institutional transformation of business organizations, however, should be understood as a path-dependent process that was influenced by traditional business practices. The introduction of corporate forms in China had established new rules of the game in organizing business, but at the same time these corporate forms provided a device that allowed some of the traditional business practices in China to be revitalized and sustained. Corporate forms provided an institutional device to consolidate capital in modern China, but it was the direct and indirect personal connections that helped to make it possible (Chung 2003).

Through subscriptions of shares from the public, the limited-liability company allows entrepreneurs to create a much bigger enterprise than those based on sole proprietorship or a partnership. At the same time, by using the governance structure of the modern corporate form, entrepreneurs can distance themselves from the shareholders – the real owner – and can gain more control of the decision-making process. Also, limited liability allows investors and, at the same time, the entrepreneurs to be able to spread out of their investments to more companies and create a much larger network.

Rather than depending solely on personal capital, a corporation with the ownership divided into shares of equal value can help the entrepreneurs to create a firm that incorporates outsiders' resources. In the context of China, individual entrepreneurs can use this 'Western' institutional design to consolidate resources that are directly or indirectly connected to oneself, with the hope that a considerable amount of total strangers will also be interested in investing in the corporation. Compared with traditional partnerships that would permit the pooling of resources only among a small group of people, corporate forms provide the institutional construct that allows more people to participate with basically any amount they are willing to invest.

Because of the particular route of economic transformation in China, entrepreneurs using Western corporate forms to organize their businesses were able to exercise a degree of control that would not be found in a Western context. Individual merchants were able to consolidate a much larger quantity of resources then before without the typical constraints from the guilds. Old practices governing interpersonal relationships continued to function, but at the same time allowed individual entrepreneurs to coordinate those resources in a more flexible way, and in a way to increase one's competitiveness in the marketplace. By relaxation of membership in modern business and trade associations, the transformation of the traditional business networks represented a broadening of the scope of possible connections (Rowe 1984). Geographical and professional dividing lines that used to exist in Chinese business communities were finally disappearing.

Since the 1920s, large business conglomerates have been formed by individual entrepreneurs in China through the creation of multiple personal networks by connecting oneself to both the traditional networks (e.g. native-bank networks) and a contemporary one (e.g. the industrialists' networks) (Li 2000). The construction of multiple layers of networks, which would transgress native places and business sectors, and now companies as well, become possible in the new institutional setting.

The Emergence of Chinese Diaspora Entrepreneurial Networks

The changes described above shed light on the changes in the institutional framework in which business was being conducted in China. The emergence of corporations signified the emergence of new economic actors. This implies a change in the business logic of the past. Capitalism developed in China, but with a logic different from that of the West.[31] Rather than replacing traditional business practices in China, the Western model of business organization – the corporate form – was modified by being incorporated with traditional Chinese networking practices. The new networking practices, which maintained the same social-trust mechanism of the traditional model, allowed for individuals to take personal advantage of the network resources.

While the Western model of business organization was being adopted almost everywhere around the world after the Second World War, the innovative use of it by the Chinese can simultaneously be found in all Chinese business communities. Companies were set up by the Chinese according to the local company law, but they were at the same time connected together, in one way or another, through personal networks. Chinese entrepreneurs who were competent further expanded their businesses by using various levels of networks.

Robert Kuok of Malaysia, for example, diversified his 'silent empire' through cross-investment in many companies that were based on his personal connections.

As described by Cottrell (1986), his empire was composed of a group of core family businesses linked to an extended network well beyond the family firms and to a wide variety of businesses. This level of networks indicates a highly diversified investment strategy, representing the kinds of personal connections that Kuok has accumulated all these years. Cottrell (1986) has documented a very complex web of companies with a wide range of businesses and with all levels of cross-investment. While the holdings in Kuok's core business were always high, with some as high as 100 per cent, the holdings of his cross-investment varied a great deal: many of them were less than 10 per cent, with some of them as low as 1 per cent.[32] These networks of investment were very likely the results of broad kinship and friendship ties, representing a way to retain all the potential business opportunities for further use.[33]

The networks continued to expand on yet another level. Chinese diaspora entrepreneurs, each with their own business conglomerates, teamed up to 'cooperate' and to explore even more business opportunities. Redding (1995) identified the fact that intensive cross-border entrepreneurial networks existed among major ethnic Chinese diaspora entrepreneurs. Based on the companies' official announcements, the business deals that were generated between 1990 and 1994 by these Chinese diaspora entrepreneurial networks in Asia amounted to tens of millions of US dollars. The network-based economy that originated in late Imperial China and has been transformed since the introduction of the Western corporate forms has further developed into an even more vibrant system among the overseas Chinese societies.

Notes

1. There is much literature describing the Chinese Diaspora economy; see for example Brown 1995; Hamilton 1996a; Kao 1993; Lever-Tracy et al. 1996; Omohundro 1983; Redding 1995; Weidenbaum and Hughes 1996; Yeung and Olds 2001.
2. For a discussion of firm-based economy, see Biggart and Hamilton 1992. For a discussion of the nature of a network-based economy, see Hamilton 1996b.
3. The network-based economy, however, is not restricted to Asia. Both general networking and ethnic-specific networking as a business strategy are also not unique to the Chinese. Italian, Jews and Greeks, for example, are commonly identified as using personal networks for business.
4. An interesting twist that is happening now is the reverse influence of the overseas Chinese capitalism on the Mainland. See, for example, Lever-Tracy et al. 1996.

5. The networks of the Chinese-owned computer firms in California, United States, for example, is a widely mentioned example of how this ethnic-based business networking can create competitive advantages (Zhou 1996).
6. While there is evidence on its significance in the region, we should, however, be careful not to exaggerate the overall role of Chinese capital within each Southeast Asia country and for the interconnectedness of these economies. A more country-specific historical sociology of ethnic Chinese enterprises should replace the notion of a pan-Southeast Asian universalism (Gomez and Hsiao 2001).
7. The smallest estimated average increase in bilateral trade in recent years in Southeast Asia in differentiated products attributable to ethnic Chinese networks is about 60 per cent (Rauch and Trindade 2002). Studies also indicate that Chinese ethnic business networks did not just extend regionally but also internationally in recent years (Yeung 1999).
8. In Southeast Asia, however, connections with the government are just as important as the ethnic ties. Social capital has to be incorporated with political capital.
9. Whether the use of *guanxi* – or personal connections – is becoming significant in the growing post-socialist economy of the Mainland China is still controversial. See Guthrie 1999 and Yang 2002.
10. This mechanism of course will never be perfect. Merchant manuals during the Ming-Qing period, for example, the *Jianghu Bidu* (Essential Reading for Travellers), constantly warned merchants about all kinds of possible dishonesties that they might come across. How to determine who is and who is not honest by their appearance, by the way they talk, etc. is a common theme of these manuals (Chen 1997; Lufrano 1997).
11. As a matter of fact, China has a very long history of using contracts in business transactions and other matters (Hansen 1995; Faure and Pang 1997). More research has to be done before reaching any conclusions, but it may possibly be true that the Chinese use contracts in situations where things can be specified, and depends less on contracts when flexibility is preferred. So it may be wrong to say that China lacks the culture of contracts, even though the base of it may still be different from that in the West.
12. If a part is needed to assemble a product, one can simply call up the business partner with a good *guanxi*. No time is needed to spend to go through all the details, e.g. price, delivery time, specification, etc., because one can assume that the best possible offer will be given (Uzzi 1997).
13. Arrighetti (1997) shows how in Western business practice, flexibility beyond contract can actually be achieved, under some conditions, on a foundation of formalized contractual understandings.

14. Traditional organizations such as lineage or native-place association in Chinese societies carry the same group dynamics described, and therefore can provide pressure on ethical conformity within the organization. In a contemporary context, however, it is certain that the in-group control of these kinds of organizations has lost most of its energy because of the weakening of group involvement and interpersonal bonds.
15. It is not because they are necessarily more trustworthy, but because the personal connection or trust is more easily established between *tongxiang* since they have either known each other for years (all coming from the same village or town), or they know people who have known the other side for years.
16. There is, however, a debate on whether Chinese social logic in business practices will eventually be replaced by Western business logic. Some suggest that *guanxi* practice will change when a more mature legal framework is developed (Landa 1994); others, however, maintain that Chinese business practices will resist change since its persistence goes beyond functional necessity (Tong and Yong 1998).
17. Studies suggest that Western firms depend on network relationships only when they are small or weaker, or those who need the benefit of networking more, but once their corporate power increase to a certain level, they will shift back to market governance (Baker 1990; Podolny and Page 1998). Also, once the firm is bigger, it has the capacity to internalize the transaction rather than depending on inter-firm exchanges which are considered to be risky. Chinese business, on the other hand, still depends on personal relationships even after they are big (e.g. Weidenbaum and Hughes 1996; Yeung 1997).
18. The analysis is based on a 1927 ownership list published by the native-bank guild included in People's Bank of China 1960: 264–8.
19. Native banks provided services similar to those of a modern bank, including services such as short-term loans, issuing guaranteed promissory notes and currency exchange.
20. In my sample it appears that many investors used to be opium traders or dyestuff merchants.
21. In a few cases, the number of partners involved was as few as two and as many as seven or eight.
22. Even if one family owned a bank, the family would expand its business by opening multiple native banks with different names and with different managers. For example, the Cheng family of Suzhou invested in twelve different banks between 1876 and 1953 through different combinations of family members (People's Bank of China 1960: 738–41).
23. The average is 100,000 taels in 1927. It used to be even less in previous decades.

24. Traditionally, the Chinese government always welcomed a 'self-regulated' economy so long as sufficient revenue could be generated. With limited administrative power, the Chinese government in the past simply granted exclusive rights to guilds, brokers (*yiahang*) or small groups of merchants to either control and regulate the market or to monopolize certain businesses (e.g. salt trade). Taxes and fees were collected from owners with exclusive rights rather than directly from every individual economic actor.
25. Chinese merchants consider it a disgrace if the bank requires a mortgage for loan. Reputation, and not property, is traditionally used as a mortgage.
26. For an excellent treatment on the transformation of business and trade associations in modern China, see Yu 1993. For an overview description of the same process in Shanghai, see Zhang 1990. For discussion on exemplars of other modern business organizations which were established during that time, see for example Bergère (1992). By 1908, there were 39 general chambers of commerce and 223 branch chambers established in China. By 1912, the total number rose to 794, and in 1915, to 1,262 (Chan 1977: 226).
27. The average age for the thirty-five directors before the reorganization in 1920 was 57.2; the average age after the reorganization dropped to 44 (Xu and Qian 1991).
28. Depending on how much capital they had, *Hui* merchants for example would usually be involved only in a few kinds of trade such as salt trading, tea trading, pawnshops, lumber, food and textiles (Wang 1997).
29. In some manufacturing sectors, for example, the number of apprentices the shop owner could have was set by the guild. In this case, the shop could rarely expand and produce more, even if more buyers could have been found.
30. The time at which business elites could emerge was usually when either a particular merchant or a particular *bang* had secured exclusive resources from the Imperial state. Hu Xiuyang, a prominent native-bank merchant in the Late Qing, became extremely rich and high-status not because of his success in his native-bank business which could be very profitable, but largely because he had extensive personal connections with high-level state officials. A lot of *Jin* merchants from the Shanxi province became very wealthy mainly because they were engaged in the salt trade in the earlier stage – a business that needed licences that were exclusively franchised by the government, and *Piaohao* at the later stage – a financial business that involved huge amounts of government remittances and deposits (Zhang 1989).
31. More and more of the literature suggests that there is more than one kind of capitalism, each coming from a different institutional tradition. See for example Whitley 1999 and Guillén 2001.
32. Another 'model' of control adopted by the Chinese family business is to establish an unlimited company as a holding company and use this company

to 'invest' and to 'own' other limited companies – many of them being public companies. With the holding company as an unlimited company, the family does not have to disclose the family asset to the government and the public, while at the same time, they can use the institution of modern business organizations – limited-liability companies – to expand and coordinate the family's business empire.

33. To invest a minimal amount of capital, in Kuok's case some as low as 1 per cent, in a friend's company is a way to maintain the *guanxi* between them that might become worthy in the future. This is also a way to expand one's business by extending the web of potential opportunities with an unlimited boundary.

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